

Washington State Auditor's Office
Accountability Audit Report

Seattle School District No. 1
King County

Report Date
March 30, 2007

Report No. 72832

Issue Date
June 22, 2007



Washington _____
State Auditor
_____ Brian Sonntag



**Washington State Auditor
Brian Sonntag**

June 22, 2007

Board of Directors
Seattle School District No. 1
Seattle, Washington

Report on Accountability for Public Resources

Please find attached our report on Seattle School District No. 1's accountability for public resources and compliance with state laws and regulations and its own policies and procedures.

In addition to this work, we also audit the District's financial statements and compliance with federal laws and regulations. The results of that audit will be included in a separately issued audit report.

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

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King County
March 30, 2007**

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Audit Summary

Seattle School District No. 1 King County March 30, 2007

ABOUT THE AUDIT

This report contains the results of our independent accountability audit of Seattle School District No. 1.

We performed audit procedures to determine whether the District complied with state laws and regulations and its own policies and procedures. We also examined District management's accountability for public resources. Our work focused on specific areas that have potential for abuse and misuse of public resources.

Areas examined during the audit were selected using financial transactions from September 1, 2005, through August 31, 2006.

RESULTS

In most areas the District complied with state laws and regulations and its own policies and procedures. However, we identified two issues significant enough to report as audit findings:

- Seattle School District No. 1's internal controls over payroll continued to be inadequate and, as a result, public funds were misappropriated and questionable payments were made.
- Seattle School District No. 1 lacked adequate controls over enrollment reporting.

We noted other issues we communicated directly to District management. We appreciate the District's commitment to resolving the issues.

RELATED REPORTS

Our opinion on the District's financial statements and compliance with federal program requirements is provided in a separate report, which includes the District's financial statements.

CLOSING REMARKS

We thank District officials and personnel for their assistance and cooperation during the audit.

Description of the District

Seattle School District No. 1 King County March 30, 2007

ABOUT THE DISTRICT

Seattle School District No. 1 serves approximately 46,600 students and operates 12 high schools, 10 middle schools, 58 elementary schools, eight kindergarten through eighth grade schools and nine alternative schools and special programs. An elected, seven-member Board of Directors oversees the District. The Board sets priorities and manages resources. The Board appoints a superintendent who oversees day-to-day operations. The District had a \$453 million operating budget for the 2005-06 school year and approximately 5,000 employees.

AUDIT HISTORY

We audit the District annually. The past three audits reported the following:

- In the 2003 audit, we reported two findings related to use of restricted revenues and payroll.
- In the 2004 audit, we did not report audit findings in the accountability audit report. We reported one finding in the report of financial statements and federal single audit.
- In the 2005 audit, we reported two findings. Cash receipts were misappropriated or lost at three schools. Associated Student Body public money was inappropriately deposited in private bank accounts.

ELECTED OFFICIALS

These officials served during the audit period:

Board of Directors:

District 1	Sally Soriano
District 2	Darlene Flynn
District 3	Brita Bulter-Wall
District 4	Michael DeBell
District 5	Mary Bass
District 6	Irene Stewart
District 7	Cheryl Chow

APPOINTED OFFICIALS

Superintendent
Chief Academic Officer
Chief Operating Officer
Legal Counsel
Executive Director of Financial Services
Accounting Manager

Raj Manhas
Carla Santorno
Mark Green
Gary Ikeda
Art Jarvis
Ronic Lirio

ADDRESS

District

2445 Third Avenue S.
Seattle, WA 98124-1165
(206) 252-0000
<http://www.seattleschools.org>

Audit Areas Examined

Seattle School District No. 1 King County March 30, 2007

In keeping with general auditing practices, we do not examine every portion of Seattle School District No. 1's financial activities during each audit. The areas examined were those representing the highest risk of noncompliance, misappropriation or misuse. Other areas are audited on a rotating basis over the course of several years. The following areas of the District were examined during this audit period:

ACCOUNTABILITY FOR PUBLIC RESOURCES

We evaluated the District's accountability in the following areas:

- Payroll
- Cash disbursements
- Petty cash and revolving accounts
- Cash receipting and revenues
- Accounts receivables
- Safeguarding of assets
- Property and equipment
- Purchase of goods and services
- Purchasing and accounts payable
- Financial statement preparation and journal entries

We audited the following areas for compliance with certain applicable state and local laws and regulations:

- Deposit and investment of public funds
- Timely deposit of public funds
- Use of restricted funds
- Risk management
- Insurance and bonding
- Budget requirements
- Ethics/conflict of interest laws
- Open Public Meetings Act
- Inter-fund transactions
- One fund benefiting at the expense of another
- Propriety of expenditures
- Legal and supported payments
- Certification and approval of expenditures
- Allowable expenditures
- Travel expenses
- Competitive bid law compliance
- Public works contracts
- State prevailing wage requirements
- Contracting for architecture and engineering, construction, purchased services and personal services
- Selection of architectural and engineering firms
- Student enrollment reporting
- Student transportation ridership reporting
- Teacher education and experience (staff mix) reporting

FEDERAL PROGRAMS

We evaluated internal controls and tested compliance with federal program requirements, as applicable, for the District's major federal programs, which are listed in the Federal Summary section of the financial statement and single audit report.

FINANCIAL AREAS

Our opinion on the District's financial statements is provided in a separate report. That report includes the District's financial statements and other required financial information. We examined the financial activity and balances of the District including:

- Cash and investments
- Revenues
- Expenditures
- Long-term debt
- Overall presentation of the financial statements

Schedule of Audit Findings

Seattle School District No. 1 King County March 30, 2007

1. **Seattle School District No. 1's internal controls over payroll continued to be inadequate and, as a result, public funds were misappropriated and questionable payments were made.**

Background

The District spent \$271 million in wages and benefits in the 2005-06 school year. We previously communicated to District management, or reported as audit findings, internal control weaknesses in the District's payroll system. The issues we previously reported included:

- 2000-01: We found employees had access to approved timesheets and some had been altered after approval. We also found some timesheets were not approved by principals before payment. We identified \$45,000 in questionable pay resulting from these weaknesses.
- 2001-02: We again found employees had access to approved timesheets. We also found the District did not have a policy on monitoring payroll to ensure hours reported were accurate. The District also did not have controls in place to ensure employees did not submit duplicate time records or controls over the reporting and recording of leave.
- 2002-03: The continued absence of controls over payroll records led to a misappropriation of \$3,886.
- 2003-04: Inadequate controls over payroll continued. An employee was overpaid \$1,873 when the employee reported the same hours twice.
- 2004-05: Continuing inadequate controls over payroll led to a loss of approximately \$12,000. The actual amount misappropriated could not be determined due to weaknesses in the District's payroll system.

Description of Condition

We noted the following continuing internal control weaknesses in the District's payroll system that led to losses or questionable payments of public funds:

- Employee access to approved Extra Time Reporting forms continued to be inadequately controlled. A teacher at Nova High School had access to these forms after they were approved and before they were submitted to payroll for processing. The teacher added hours to the approved time sheet. The District reviewed Extra Time Reporting forms for the last five school years and concluded the amount overpaid to the teacher was at least \$119,478. The District believes the total overpaid since 1992 could be as much as \$179,478.
- Monitoring of Time Reports, where schools record paid time off, were inadequate and did not ensure an employee's leave balance was properly reduced. From September 2004 to August 2006, a middle school under reported a teacher's use of leave by 237

hours. The teacher did not have sufficient leave to cover this time and was overpaid \$8,387.

- The District did not adequately monitor the location of and compensation to centrally-funded special education instructional assistants. In December 2006, the District's Human Resources Department discovered it could not account for an employee's location for a period of several months. When questioned, the employee stated he was on paid leave from October through early December. However, the employee did not complete the appropriate paperwork requesting use of leave benefits nor was the time properly recorded on the Time Report and his leave balance reduced. The employee received regular pay of \$6,284 for the months of October, November and early December 2006 when he did not work.
- Employees could submit more than one Extra Time Reporting form for the same hours to different supervisors. A teacher working at an alternative high school and at the evening school program submitted Extra Time Reporting forms claiming the same hours more than once and the teacher was overpaid for 17 hours or \$453.

Additionally:

- We examined records supporting approximately \$157,000 paid to nine teachers and classified staff for time worked beyond the regularly scheduled work day. We found a vocational education teacher was overpaid \$352 because of uncorrected mathematical errors on an Extra Time Reporting form. A classified employee was overpaid \$335 because three hours already had been paid and 17.5 hours of leave was recorded on two Extra Time Reporting forms. Rather than deducting those hours, the employee was paid as extra time. Payroll Services could not locate Extra Time Reporting forms supporting 66.5 hours paid to two employees.
- An employee provided false information on a job application, resulting in compensation at a rate higher than what was appropriate. The same employee claimed and was paid for jury duty when she did not serve on a jury. From September 2001 to January 2007 the employee was overpaid \$4,507.

Further, the District continued to fail to immediately notify the State Auditor's Office of all known or suspected losses as required by state law.

Cause of Condition

The District's operations are highly decentralized, and it has not adequately enforced policies and procedures over payroll processing and monitoring. The District also has not changed policies and procedures as necessary to eliminate internal control weaknesses. Although, due to the timing of our audits and audit recommendations, the District often cannot fully correct deficiencies noted during an audit in the following year. We have reported the same payroll weaknesses for the last five years.

Effect of Condition

Public funds were misappropriated, depriving the District of the use of these funds for legitimate public purposes.

We refer these matters to the King County Prosecuting Attorney's Office for any action deemed appropriate.

Recommendation

We recommend the District establish effective internal controls over payroll. The internal controls should be designed to monitor expenditures to safeguard public resources. These internal controls could include, but are not limited to:

- Requesting principals submit approved time records directly to Payroll Services, which minimizes the opportunity to falsify approved records. Controls should be designed to detect and prevent duplicate reporting of extra hours and to ensure information is mathematically correct.
- Requiring detailed and timely review of budget reports to ensure actual salary expenditures are reasonable.
- Following up on irregularities in extra compensation in a timely manner to ensure the extra hours claimed are appropriate before making payments.

We further recommend the District seek recovery from District employees and its insurance bonding company, as appropriate, of misappropriated funds and related audit/investigation costs. Any compromise or settlement of this claim must be approved in writing by the Attorney General and State Auditor as directed by RCW 43.09.330.

We also recommend the District immediately notify the State Auditor's Office of all known or suspected losses of public funds or assets or other possible illegal activity pursuant to state law.

District's Response

The District discovered the fraudulent incident involving the teacher at Nova High School when the new principal of Nova High School was reviewing the school's budget. The District has turned over the case to the Seattle Police Department and awaits possible legal proceedings. Similarly, the District attempts to recover any loss funds through a combination of legal proceedings, settlements and/or its insurance company. In cases of malfeasance, the District will seek in writing the approval of the State Auditor and Attorney General prior to any settlement.

The District concurs with the State Auditor's finding. Over the last several years, the District has noted the weakness in its internal controls surrounding the payroll cycle and continues to take the necessary steps to address the internal control weakness and the needs of a decentralized organization with a large employee base located at multiple sites across an area the size of the city of Seattle. The following are specific steps the District has or will take:

- *This summer, the WISE project culminates after several years of planning and implementation wherein the District will convert the Human Resource & Payroll systems onto the same platform as the financial system. This conversion along with changes in our business processes will address numerous internal control issues as well as make our data easier to understand and analyze.*
- *The District also has re-organized its Human Resource and Payroll Departments to better serve the needs of a decentralized organization. The new department will help standardize processes and enhance communication with its internal customers and other departments thereby helping remove the silo that has plagued the District and help identify abnormal practices and transactions.*
- *The District continues to train managers to monitor their budgets and ensure actual salary expenditures are reasonable. In the spring of 2007, central managers were required to attend these training sessions.*

- *The District has created an Internal Auditor position that will be responsible for ensuring the District complies with its own policies and procedures as well as all related local, state, and federal laws.*

In addition, the District will ensure the timely notification of all known or suspected losses to State Auditor's Office by communicating this requirement District wide and create the necessary channels with the new Internal Auditor to facilitate such timely communication.

Auditor's Remarks

We thank District officials for their assistance and cooperation during this audit.

Applicable Laws and Regulations

RCW 43.09.185 – Loss of public funds-Illegal activity – Report to state auditor's office.

State agencies and local governments shall immediately report to the State Auditor's Office known or suspected loss of public funds or assets or other illegal activity.

Schedule of Audit Findings

Seattle School District No. 1 King County March 30, 2007

2. The District lacked adequate controls over enrollment reporting.

Background

The Office of Superintendent of Public Instruction (OSPI) establishes the rules and provides instructions on how school districts should report enrollment for state funding. Students are funded based on the number of hours per week they are enrolled in school and must meet certain attendance requirements in order to be counted. A high school student enrolled at least 25 hours each week is considered full time and counted as one full-time equivalent (FTE) for funding purposes. In addition, students must have attended school one of the first four days of September or not been absent for 20 consecutive days at count dates in October through May to be eligible for funding.

In the 2006 school year, the District reported 45,599 students and received approximately \$196 million in combined state enrollment and staff mix funding.

Description of Condition

The District misreported students due to:

- Counting all students at 10 of 11 high schools audited as full time in September regardless of the number of hours the students were enrolled. Students enrolled less than 25 hours per week must be reported as part time. The District over reported 267.15 monthly FTEs due to this error.
- Counting full-time Running Start students who were not enrolled in classes at the high schools as enrolled full time in September. The District over reported 93.0 monthly FTEs due to this error.
- Counting students who did not attend one of the first four days of September. The District over reported 19.0 FTEs due to this error.

Cause of Condition

The District does not have procedures in place to ensure only eligible students are reported as enrolled or that actual hours of scheduled class time is used in the calculation of student hours.

Effect of Condition

The District over reported 379.15 monthly student FTEs in fiscal year 2006 and received \$200,967.13 more funding than it was entitled to receive.

Recommendation

We recommend the District establish and follow controls to ensure:

- Student counts are based on actual hours of enrollment.
- Only those students who attended school one of the first four days of September are reported.

We also recommend the District review its enrollment, based on the errors identified, and submit corrected enrollment reports to OSPI for fiscal year 2007.

District's Response

The District concurs with this finding with clarification that the enrollment finding is limited to the month of September 2005. The issue was brought upon by an internal misunderstanding that September counts were not official, and therefore, high schools had not taken the time to correct the count for schedule changes, absentees and running start students. In addition, the District has clear and appropriate procedures in place to make accurate enrollment counts from October through May of each school year as proven by prior enrollment audits.

The District revised its procedures to ensure the September enrollment count is accurate prior to reporting to OSPI. Principals, registrars and personnel responsible for the accuracy of the enrollment figures have been notified of these revised procedures.

In addition, the District has corrected the enrollment count for September 2006 and amended its numbers with OSPI.

Auditor's Remarks

We thank the District for its cooperation and assistance during the audit and look forward to reviewing the District's corrective action during our next audit.

Applicable Laws and Regulations

Washington Administrative Code (WAC) 392-121-106 provides the definition of an enrolled student and identifies the requirement for attending one of the first four days of September. It states in part:

- (4) Actually participated on a school day during the first four school days of the current school term, or on a school day during the current school term on or prior to the date being counted.

Washington Administrative Code (WAC) 392-121-122 provides the definition of a full-time equivalent student and minimum hours necessary to be counted as a full time student. It states in part:

. . . hours . . . inclusive of class periods and normal class change passing time, but exclusive of noon intermissions.

- (1) The minimum hours for each grade . . .
(e) Secondary (grades 7 through 12); 25 hours each week . . .

- (2) A student enrolled for less than the minimum hours . . . shall be counted as a partial full-time equivalent student equal to the student's hours of enrollment divided by the minimum hours for the student's grade level

Status of Prior Audit Findings

Seattle School District No. 1 King County March 30, 2007

The status of findings contained in the prior years' audit reports of the District is provided below:

1. Seattle School District No. 1's cash receipts were misappropriated or lost at three schools.

Report No. 70857, dated March 31, 2006

Background

Employees at Salmon Bay, Dearborn Park and West Seattle schools did not deposit all public funds received from students. The employees did not follow District cash-handling policies and procedures. Due to inadequate monitoring, District management did not detect two of the three losses in a timely manner. Lunchroom deposits, totaling at least \$1,322 at Salmon Bay and \$400 at Dearborn Park, were not accounted for. Staff at West Seattle lost approximately \$480 in art fees.

Status

To verify money collected in lunchrooms is deposited in a timely manner, the Child Nutrition Services (CNS) office reviews the driver pick-up logs and follows up as needed. The District's Accounting Department reviews deposit data and shares it with CNS staff if late deposits are found. Twice monthly, CNS reconciles lunchroom bank deposits to point-of-sale records for all of the District's schools. CNS distributed policies and procedures to staff and, in some instances, provided one-on-one training to employees. While we appreciate the District's efforts to educate staff with cash-handling duties, in the 2006-07 school year two more schools lost lunchroom cash receipts. Approximately \$422 was misappropriated at Sealth High School and \$417 from Whitman High School. At these schools, cash was not physically secure, which provided an opportunity for someone to take the funds from the school offices. Since school staff and others had access to the area where the funds were kept, the District cannot determine who was responsible for the loss. The District should remind staff about the importance of securing cash and should enforce its cash-handling policies and procedures.

2. Seattle School District No. 1's Associated Student Body (ASB) public money was inappropriately deposited in private bank accounts.

Report No. 70857, dated March 31, 2006

Background

At least \$96,011 in public funds, raised by students and District employees, was not deposited into a District bank account. The money was deposited into private bank accounts that were wholly or partly controlled by coaches or parents. This condition places ASB funds at risk of misuse, loss or misappropriation and hinders the District's ability to ensure the money is used for an appropriate purpose and for the benefit of students.

Status

The Accounting Manager, Accounts Payable Supervisor and ASB Fund Analyst attended an ASB workshop in August 2006. At the beginning of the 2006-07 school year, the District disseminated ASB requirements to principals. Management sent the audit findings to the affected organizations. District Accounting continues to work with individual school principals, fiscal secretaries, the Parent Teacher Association and booster clubs to ensure ASB money is deposited in ASB accounts in accordance with state law and District policies. District Accounting is tracking ASB revenues for each school to ensure deposits are made in a timely manner and to detect and resolve noncompliance immediately.